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In the Supreme Court of the United States

OCTOBER TERM, 1996

FIRST JERSEY SECURITIES, INC., ET AL., PETITIONERS

v.

SECURITIES AND EXCHANGE COMMISSION

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE SECURITIES AND EXCHANGE COMMISSION IN OPPOSITION

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QUESTIONS PRESENTED

1. Whether, in enforcement actions brought by the Securities and Exchange Commission, the federal courts' statutory authority to enjoin violations of the securities laws includes the ancillary equitable authority to order disgorgement of profits the defendants obtained as a result of their wrongdoing.

2. Whether the court of appeals properly held petitioner Brennan jointly and severally liable for the disgorgement.

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-47a) is reported at 101 F.3d 1450. The opinion of the district court (Pet. App. 48a-104a) is reported at 890 F. Supp. 1185. The district court's findings of fact (Pet. App. 105a-218a) are unreported.

JURISDICTION

The court of appeals entered its judgment on December 10, 1996. A petition for rehearing was denied on February 27, 1997. Pet. App. 219a-220a. The petition for a writ of certiorari was filed on May 23, 1997. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. Section 20(b) of the Securities Act of 1933 (Securities Act) provides that, "[w]henever it shall appear to the [Securities and Exchange] Commission that any person is engaged or about to engage in any acts or practices which constitute or will constitute a violation of the provisions of [the Act], or of any rule or regulation prescribed under authority thereof," the Commission may bring an action in federal court "to enjoin such acts or practices." 15 U.S.C. 77t(b). Section 21(d) of the Securities Exchange Act of 1934 (Exchange Act) contains a virtually identical provision. 15 U.S.C. 78u(d).

2. a. Petitioner Robert E. Brennan founded petitioner First Jersey Securities, Inc. (First Jersey) in 1974 as a discount broker-dealer specializing in the underwriting, trading, and distribution of low-priced securities. Pet. App. 3a.[1] At all relevant times, Brennan was both a director and the sole owner of First Jersey. From January 1982 to August 1985, Brennan also served as First Jersey's president. In September 1985, Brennan became First Jersey's chairman and chief executive officer. *Id.* at 6a.

Brennan was intimately involved in the day-to-day operations of First Jersey. He decided which securities First Jersey would underwrite and was involved in setting their prices. Pet. App. 7a. He participated in the formulation of the firm's pricing policies, regularly reviewed research reports on securities, and discussed with his staff First Jersey's compliance with rules regulating the securities trade. *Ibid.*

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[1] Petitioners do not challenge the district court's findings of fact.

b. From 1982 to 1985, "First Jersey, with Brennan at the helm, * * * employed a massive and coordinated system of fraudulent practices to induce its customers to buy certain securities from [First Jersey] at excessive prices unrelated to prevailing market prices." Pet. App. 3a. Petitioners hired hundreds of salespersons to carry out the scheme, seeking out prospective employees who had no prior experience in the securities business. *Id.* at 3a-5a.[2]

The fraudulent scheme generally operated as follows: Every month, each of petitioners' 32 domestic branch offices focused its efforts on selling one security, which was selected by First Jersey's home office. The salespersons contacted prospective buyers through "cold calls" to individuals who were not First Jersey customers and whose names were found in general directories. Pet. App. 4a. Follow-up calls were made to promising contacts with scripted sales pitches designed to close the sale of the selected security. *Ibid.* Petitioners designed the system to keep the salesforce uninformed about the securities they sold and indifferent to the needs and desires of customers. Salespersons were discouraged from conducting independent research, deviating from the scripted sales pitches, or promoting other securities. See *id.* at 4a-5a, 53a, 60a-61a. Petitioners tied compensation almost exclusively to success in selling the designated securities. *Id.* at 5a.

Petitioners employed this system to sell the six issues of securities involved here from one set of branch offices, to buy those securities back immedi-

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[2] The district court found that typical hires included a waiter, a bellman in a Playboy club, and a convenience store worker. Pet. App. 51a n.4.

ately from the original customers, and then to resell the securities through a different set of branch offices to a new group of customers, at prices up to 150% or more above the prices at which the securities had just been repurchased. Pet. App. 5a-6a. At each stage of the process—initial sale, repurchase, and resale—salespersons used scripts prepared and disseminated by petitioners to deceive the customers into believing that the transactions were occurring in a freely operating market and at market-determined prices. In fact, the market and the prices for the securities were created and controlled by First Jersey. As a result, the initial group of customers sold the securities back to First Jersey without being informed that the securities were to be immediately resold at a much higher price, while the second group purchased the securities at prices that were artificially inflated. *Id.* at 8a, 67a. Petitioners' fraud netted more than $27 million in unlawful profits. *Id.* at 13a.

3. In 1985, the Commission filed suit against petitioners, alleging that the sales scheme resulted in fraud on First Jersey's customers, in violation of Section 17(a) of the Securities Act, 15 U.S.C. 77q(a), Section 10(b) of the Exchange Act, 15 U.S.C. 78j(b), and Rule 10b-5, 17 C.F.R. 240.10b-5.

Following a 41-day bench trial, the district court concluded that the Commission had "overwhelmingly proven" (Pet. App. 96a) that petitioners violated the antifraud provisions of the securities laws, both by withholding from customers the true nature of the First Jersey-created and -controlled market in which the transactions occurred and by charging fraudulently excessive markups on the securities. *Id.* at 67a-73a. The district court found that petitioners'

conduct "was entirely purposeful" and that they "orchestrated every facet" of First Jersey's operations to ensure that the securities "were sold *when* they wanted—*where* they wanted—at prices determined not by market forces but by First Jersey itself." *Id.* at 66a-67a. Moreover, the evidence "overwhelmingly established that [petitioners] wilfully and deliberately violated established law forbidding excessive mark-ups." *Id.* at 70a.

With respect to petitioner Brennan's personal responsibility for the fraudulent conduct, the district court found that petitioner was a " 'hands-on' manager who was intimately involved in the operations of First Jersey, including all significant decisions regarding the firm's underwriting, retail sales and trading activities." Pet. App. 78a; see also *ibid.* (finding that petitioner personally signed each of the underwriting agreements at issue in the case).[3] Because petitioner Brennan exercised such close control over the company's operations and personally participated in the operation of the fraudulent scheme, the district court found him liable as a primary violator of the antifraud provisions. *Id.* at 80a. The court also ruled that Brennan was jointly and severally liable as a "control person" of First Jersey, under Section 20(a) of the Exchange Act, 15 U.S.C. 78t(a). Pet. App. 80a-81a.[4] The court noted that petitioner "possessed con-

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[3] Petitioner Brennan never contended that the sales practices and price mark-ups were attributable to the unauthorized actions of other executives of First Jersey. Pet. App. 79a.

[4] Section 20(a) provides that any person who "controls any person liable under any provision of [the Exchange Act]" is "jointly and severally" liable to the same extent as the controlled entity, subject to a good-faith defense. 15 U.S.C. 78t(a).

trol over every aspect of First Jersey's operations" and that petitioner had "virtually conceded" his status as a control person at trial. *Id.* at 81a.

The district court enjoined petitioners from further violations of the antifraud provisions of the securities laws. Pet. App. 96a-98a. The court found it "highly likely that future violations might occur" (*id.* at 98a) because (i) petitioners' violations of the securities laws were "flagrant and deliberate," (ii) "[petitioner] Brennan is completely without remorse for the violations proven in this case," and (iii) even after their fraudulent scheme was uncovered, petitioners "continued to carry on business activities in the securities industry * * * offending various federal and state securities laws." *Id.* at 97a. In addition, the court ordered petitioners to disgorge $22 million in profits they obtained in the fraudulent scheme, along with prejudgment interest. *Id.* at 99a-102a.[5] The court held petitioners jointly and severally liable for the disgorgement, because they were each individually and primarily liable for the violations that occurred and because Section 20(a) imposes joint and several liability on Brennan as a control person of First Jersey. *Id.* at 101a. The court directed the Commission to "submit plans for disposition" of the disgorgement fund, and provided that those plans may include "a Court-approved plan of distribution." *Id.* at 225a.[6]

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[5] Although the district court found that petitioners enjoyed more than $27 million in wrongful profits, the disgorgement award was reduced to reflect the $5 million paid by petitioners to settle a class action. Pet. App. 13a.

[6] The district court also appointed a special agent to examine whether other violations occurred. Pet. App. 103a. The court of appeals reversed that aspect of the district court's

4. The court of appeals affirmed. Pet. App. 1a-47a. The court of appeals found no error in the district court's imposition of liability on petitioners for securities fraud violations. *Id.* at 21a-37a. With respect to the ordered disgorgement, the court of appeals held that the amount of disgorgement "is a reasonable approximation of First Jersey's unlawful profits from its fraudulent transactions and is not punitive in nature." *Id.* at 39a.

The court of appeals also rejected petitioner Brennan's claim that joint and several liability for the disgorgement was improperly imposed. The court noted that petitioner was both "primarily liable for the frauds at issue here, having been 'intimately involved' in their perpetration, and is also liable as a controlling person of First Jersey." Pet. App. 40a. In rejecting petitioner Brennan's contention that he should be required to disgorge only the exact amounts that he withdrew from the firm, the court of appeals stated that the contention "might be more persuasive if he had owned less than all of First Jersey's stock." *Ibid.* But since he was the firm's sole and complete owner, full liability for the disgorgement was appropriate: "[T]o the extent that the Firm's net worth was increased by its unlawful activities, so was Brennan's personal wealth." *Ibid.*

ARGUMENT

Petitioners do not challenge their legal responsibility for millions of dollars in securities fraud targeted at unsophisticated investors. Nor do they dispute the extensive factual findings chronicling their respon-

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order (*id.* at 44a-47a), and we have not sought review of that issue.

sibility for the fraud at issue and their perpetration of additional, unlawful financial schemes during the pendency of the present Commission proceeding. See Pet. App. 83a-93a (chronicling nearly twenty years of "regulatory agency brushes"). Petitioners seek this Court's review solely of the questions whether they may retain the profits of their wrongdoing and whether Brennan can escape Congress's imposition of joint and several liability. Because the court of appeals' decision is consistent with the decisions of this Court and other circuits and turns upon the unique factual circumstances surrounding petitioners' fraud, this Court's review is not warranted.

1. Petitioners contend (Pet. 7-21) that the court of appeals erred in concluding that federal courts may order disgorgement in Commission actions under Section 20(b) of the Securities Act, 15 U.S.C. 77t(b), and Section 21(d) of the Exchange Act, 15 U.S.C. 78u(d). That claim does not merit further review for three reasons.

a. First, as petitioners concede (Pet. 7), every court of appeals that has addressed the question has construed the relevant statutory provisions to authorize an order of disgorgement as ancillary to the authority to grant injunctive relief. See, *e.g.*, *SEC* v. *Bilzerian*, 29 F.3d 689, 696-697 (D.C. Cir. 1994); *SEC* v. *AMX, Int'l, Inc.*, 7 F.3d 71, 76 n.8 (5th Cir. 1993); *SEC* v. *Rind*, 991 F.2d 1486, 1490 (9th Cir.), cert. denied, 510 U.S. 963 (1993); *SEC* v. *Ridenour*, 913 F.2d 515, 517-518 (8th Cir. 1990); *SEC* v. *Blavin*, 760 F.2d 706, 712-713 (6th Cir. 1985); *SEC* v. *MacDonald*, 699 F.2d 47, 54 (1st Cir. 1983) (en banc); see also *Commodity Futures Trading Comm'n* v. *American Metals Exchange Corp.*, 991 F.2d 71, 76 n.9 (3d Cir. 1993) (acknowledging availability of disgorgement as

ancillary relief under securities laws).[7] Petitioner cites no court decision, nor are we aware of any, that has ruled otherwise.

b. Second, the court of appeals' ruling fully adheres to this Court's precedents. This Court has repeatedly held that, "[w]hen Congress entrusts to an equity court the enforcement of prohibitions contained in a regulatory enactment, it must be taken to have acted cognizant of the historic power of equity to provide complete relief," including the ordered return of ill-gotten gains. *Mitchell* v. *Robert DeMario Jewelry, Inc.*, 361 U.S. 288, 291-292 (1960) (ancillary authority to order reimbursement when Congress authorizes the issuance of injunctions); see also *Mills* v. *Electric Auto-Lite Co.*, 396 U.S. 375, 386-391 (1970); *Porter* v. *Warner Holding Co.*, 328 U.S. 395, 398-399 (1946) (order for restitution of illegal rents inheres in statutory authority to grant injunctive relief); *Clark* v. *Smith*, 38 U.S. (13 Pet.) 195, 203 (1839); cf. *Deckert* v. *Independence Shares Corp.*, 311 U.S. 282, 288 (1940) (construing jurisdictional provision of the Securities Act, 15 U.S.C. 77v).

Ordering disgorgement of the profits of wrongdoing falls within the historic scope of a court's injunctive authority. "Nothing is more clearly a part of the subject matter of a suit for an injunction than the recovery of that which has been illegally acquired and which has given rise to the necessity for

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[7] Although the Eleventh Circuit has not yet directly ruled on the question, it presumably would follow *SEC* v. *Blatt*, 583 F.2d 1325, 1335 (5th Cir. 1978), in recognizing the availability of such relief. See *Bonner* v. *City of Prichard*, 661 F.2d 1206, 1209 (11th Cir. 1981) (en banc) (adopting as binding precedent all decisions of the former Fifth Circuit issued before October 1, 1981).

injunctive relief." *Porter*, 328 U.S. at 399.[8] Indeed, courts have characterized disgorgement as "a continuing injunction in the public interest." *AMX, Int'l*, 7 F.3d at 76 n.8; see also *SEC* v. *Huffman*, 996 F.2d 800, 803 (5th Cir. 1993).

Petitioners' suggestion that this Court's precedents are "outmoded" (Pet. 18) provides no basis for review. Petitioners identify no Justice, let alone Court opinion, that has called for overruling the Court's century-old precedents regarding the scope of the federal courts' injunctive power. To the contrary, this Court has continued to apply *Porter* and its principles. See, *e.g.*, *California* v. *American Stores Co.*, 495 U.S. 271, 295 (1990) ("[W]hen Congress endows the federal courts with equitable jurisdiction, Congress acts aware of this longstanding tradition of flexibility."); *Amoco Production Co.* v. *Village of Gambell*, 480 U.S. 531, 542 (1987); *United States* v. *Rodgers*, 461 U.S. 677, 708 (1983); *Weinberger* v. *Romero-Barcelo*, 456 U.S. 305, 313-318 (1982); *Califano* v. *Yamasaki*, 442 U.S. 682, 705 (1979); *Renegotiation Board* v. *Bannercraft Clothing Co.*, 415 U.S. 1, 19 (1974); *Mitchell*, 361 U.S. at 291-292.

Petitioners devote much energy to attacking the validity of *J.I. Case Co.* v. *Borak*, 377 U.S. 426 (1964) (see Pet. 18-20), which, in part, addressed the implication of statutory causes of action. Petitioners complain that, in finding an implied cause of action under

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[8] Petitioners attempt to distinguish *Porter* on the ground that the statute in that case empowered the court to enter an "injunction, *or other order*," while the statute in this case does not refer to "other order[s]." Pet. 11. This Court has already rejected that argument. See *Renegotiation Board* v. *Bannercraft Clothing Co.*, 415 U.S. 1, 19 (1974); *Mitchell*, 361 U.S. at 291.

the proxy provisions of the Exchange Act, *Borak* relied on "generalized statutory purpose rather than the actual language" (Pet. 18), and they assert that this aspect of *Borak* provides the sole foundation for the "mother circuit['s]" "seminal disgorgement case" (Pet. 7, 11), *SEC* v. *Texas Gulf Sulphur Co.*, 446 F.2d 1301 (2d Cir.), cert. denied, 404 U.S. 1005 (1971), which the other circuits simply have "uncritically followed" (Pet. 8).

Petitioners' argument is mistaken and, indeed, "mirrors the very misunderstanding over the difference between a cause of action and the relief afforded under it" that this Court identified in *Franklin* v. *Gwinnett County Public Schools*, 503 U.S. 60, 69 (1992). *Borak*'s analysis of whether a cause of action existed is "analytically distinct" from the question presented here (and in the preceding disgorgement cases) of what relief is available for the Commission's established cause of action. *Davis* v. *Passman*, 442 U.S. 228, 239 (1979). It is thus not surprising that, despite petitioners' attempted linkage, *Texas Gulf Sulphur* never cited or relied upon *Borak*'s cause of action analysis. The court of appeals relied, instead, upon longstanding precedent from this Court, which petitioners do not challenge, regarding the scope of the federal courts' equitable powers. See *Texas Gulf Sulphur*, 446 F.2d at 1307 (citing *Mitchell*, *supra*; *Porter*, *supra*, and other cases); see also *SEC* v. *Blatt*, 583 F.2d 1325, 1335 (5th Cir. 1978).[9]

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[9] In *Franklin*, 503 U.S. at 68, this Court relied on the portion of *Borak* that addresses the remedies available for a recognized cause of action. Thus, even had the court of appeals invoked *Borak*, this Court's decision in *Franklin* belies petitioners' argument that *Borak*'s analysis regarding the remedies courts may order is "outmoded."

Irrelevant for the same reason is petitioners' reliance on *Touche Ross & Co.* v. *Redington*, 442 U.S. 560 (1979); *Central Bank of Denver, N.A.* v. *First Interstate Bank of Denver, N.A.*, 511 U.S. 164 (1994); *Northwest Airlines, Inc.* v. *Transport Workers Union*, 451 U.S. 77 (1981); and *Transamerica Mortgage Advisors, Inc.* v. *Lewis*, 444 U.S. 11 (1979). See Pet. 13, 14 n.11, 19, 20. Each of those cases addressed the existence of a particular cause of action, not the remedies available for recognized causes of action. In short, petitioners seek review of a mode of statutory construction that simply is not implicated in this case.

c. Third, Congress has repeatedly affirmed its intention that disgorgement be available as a remedy under the securities laws. As an initial matter, Congress enacted Section 20(b) of the Securities Act, 15 U.S.C. 77t(b), and Section 21(d) of the Exchange Act, 15 U.S.C. 78u(d), against the backdrop of cases (discussed above) acknowledging the historic scope of the federal courts' power to issue injunctions and accompanying ancillary relief. See *American Stores*, 495 U.S. at 295; *Romero-Barcelo*, 456 U.S. at 313 ("These commonplace considerations applicable to cases in which injunctions are sought in the federal courts reflect a practice with a background of several hundred years of history, a practice of which Congress is assuredly aware.") (internal quotation marks and citation omitted); *Mitchell*, 361 U.S. at 291-292 ("When Congress entrusts to an equity court the enforcement of prohibitions contained in a regulatory enactment, it must be taken to have acted cognizant of the historic powers of equity to provide complete relief."); *Porter*, 328 U.S. at 398 ("[T]he comprehensiveness of this equitable jurisdiction is not to be

denied or limited in the absence of a clear and valid legislative command. * * * 'The great principles of equity, securing complete justice, should not be yielded to light inferences or doubtful construction.'") (quoting *Brown* v. *Swann*, 35 U.S. (10 Pet.) 497, 503 (1836)). When Congress employs terminology in a statute "in which [is] accumulated the legal tradition and meaning of centuries of practice, it presumably knows and adopts the cluster of ideas that were attached to each borrowed word." *Evans* v. *United States*, 504 U.S. 255, 259 (1992); see also *Field* v. *Mans*, 116 S. Ct. 437, 443 (1995).

Congress, moreover, has enacted four statutes strengthening the Commission's remedial powers since 1984. Insider Trading Sanctions Act of 1984 (ITSA), Pub. L. No. 98-376, 98 Stat 1264; Insider Trading and Securities Fraud Enforcement Act of 1988 (ITSFEA), Pub. L. No. 100-704, 102 Stat. 4677; Securities Enforcement Remedies and Penny Stock Reform Act of 1990 (Remedies Act), Pub. L. No. 101-429, 104 Stat. 931; Private Securities Litigation Reform Act of 1995 (Litigation Reform Act), Pub. L. No. 104-67, 109 Stat. 737. Two of those statutes—ITSFEA and the Litigation Reform Act—contain provisions expressly recognizing that courts may order disgorgement in Commission actions brought under Section 21(d) of the Exchange Act.

ITSFEA added Section 20A(b)(2), 15 U.S.C. 78t-1(b)(2), to the Exchange Act. Subsection (b)(2) is entitled "Offsetting disgorgements against liability," and it provides that damages awarded in a private action to recover for insider trading

> shall be diminished by the amounts, if any, that [the violator] may be required to *disgorge, pursuant to a court order obtained at the instance of the Commission, in a proceeding brought under section 21(d) of* [*the Exchange Act*] relating to the same transaction or transactions.

Ibid. (emphasis added).

Similarly, Section 103(b)(2) of the Litigation Reform Act amended Section 21(d) of the Exchange Act to include a provision entitled "Prohibition of attorneys' fees paid from commission disgorgement funds." 15 U.S.C. 78u(d)(4) (Supp. I 1995). That provision states:

> Except as otherwise ordered by the court upon motion by the Commission, * * * funds *disgorged as the result of an action brought by the Commission in 'Federal court* * * * shall not be distributed as payment for attorneys' fees or expenses incurred by private parties seeking distribution of the disgorged funds.

Ibid. (emphasis added).

Those provisions' express references to the existence of a disgorgement remedy in civil actions commenced by the Commission leave no doubt that Congress considers the injunctive authority granted in Sections 20(b) and 21(d) to include the historically acknowledged, ancillary power to order disgorgement. Congress's enactment of legislation premised on its understanding of an existing statute and affirmative ratification of the established construction is compelling evidence of the statute's proper meaning. See, *e.g.*, *Loving* v. *United States*, 116 S. Ct. 1737, 1749 (1996) (passage of a statute premised on a particular

construction of an existing statute "is entitled to great weight in statutory construction"); *Commodity Futures Trading Comm'n* v. *Schor*, 478 U.S. 833, 846 (1986) (where Congress ratifies an administrative interpretation of a statute "with positive legislation, we cannot but deem the construction virtually conclusive") (internal quotation marks omitted); cf. *Musick, Peeler & Garrett* v. *Employers Insurance of Wausau*, 508 U.S. 286, 293 (1993). Petitioners' proposed construction of the Securities Act and the Exchange Act, by contrast, would render these express references to disgorgement superfluous and nonsensical. See *Field*, 116 S. Ct. at 442 n.7 (statute should be construed to avoid rendering other sections "nonsensical"); *Babbitt* v. *Sweet Home Chapter of Communities for a Great Oregon*, 115 S. Ct. 2407, 2413 (1995) (noting judicial "reluctance to treat statutory terms as surplusage").

In addition to these express statutory confirmations of the scope of courts' equitable power under Sections 20(b) and 21(d), the legislative histories of the ITSA, ITSFEA, and the Remedies Act demonstrate that Congress has legislated new remedies with the understanding that disgorgement was already available. ITSA's authorization of civil money penalties for insider trading violations built upon the preexistence of a disgorgement remedy:

> Perhaps the most widely-used remedy is the Commission's authority to bring actions in U.S. district courts to enjoin violations of the federal securities laws. * * * Once the equity jurisdiction of a court has been invoked on a showing of a securities violation, the court possesses the necessary power to fashion an appropriate remedy.

> Thus, the Commission may request that the court order certain equitable relief, *such as the disgorgement (giving up) of illegal profits.*

H.R. Rep. No. 355, 98th Cong., 1st Sess. 6-7 (1983) (emphasis added); see also *id.* at 7 ("The principal, and often effectively only, remedy available to the Commission against insider trading is an injunction against further violations of the securities laws and disgorgement of illicit profits."); *id.* at 8 ("The new penalty may be used in addition to existing remedies available to the Commission," such as "disgorgement of ill-gotten gains.").

The legislative history of ITSFEA again reveals Congress's recognition of the availability of disgorgement as a remedy and Congress's legislative reliance upon the existence of that relief for violations of the securities laws. See H.R. Rep. No. 910, 100th Cong., 2d Sess. 11 (1988) ("The creation of a new civil penalty [under ITSA] was intended to go beyond disgorgement of illegal profits to add the imposition of a significant fine as a needed deterrent," and ITSFEA builds upon that remedial foundation).

Finally, the Remedies Act authorizes "federal courts to order the payment of civil money penalties, in addition to disgorgement, for a broad range of violations of the federal securities laws." H.R. Rep. No. 616, 101st Cong., 2d Sess. 13 (1990). The section of the House Report entitled "Civil Money Penalties And Disgorgement" further noted:

> Currently, even a violator who is caught is required merely to give back his gains with interest, leaving him no worse off financially than if he had not violated the law. The Committee therefore concluded that authority to seek or impose sub-

> stantial money penalties, *in addition to disgorgement of profits*, is necessary for the deterrence of securities law violations that otherwise may provide great financial returns to the violator.

Id. at 17 (emphasis added).[10]

The Remedies Act also authorizes the Commission to order disgorgement in its administrative proceedings. See Exchange Act, § 21B(e), 15 U.S.C. 78u-2(e). The House Report's discussion of that new remedy observes that "[t]he Commission, of course, will continue to be able to seek disgorgement in its civil injunctive actions." H.R. Rep. No. 616, *supra*, at 35. Thus, petitioners' argument (Pet. 13-15) that the express authorization of disgorgement in administrative proceedings precludes a construction of Sections 20(b) and 21(d) that would allow such relief in civil actions gets congressional intent exactly backwards. The Remedies Act was designed to extend the Commission's well-established disgorgement authority in civil actions to the administrative arena.

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[10] See also H.R. Rep. No. 616, *supra*, at 22 ("[Court ordered civil money] penalties could be imposed in addition to orders of disgorgement directing a defendant to return the full amount of profits derived from a violation."); *id.* at 31 ("While Section 20 [of the Securities Act] currently does not refer to any form of civil relief other than an injunction, courts have recognized that, in Commission actions, they have the inherent power to order disgorgement, appointment of a receiver, or a prohibition against acting as a director or officer of reporting companies."); *ibid.* ("By specifying this particular type of ancillary relief, the section does not restrict the court's inherent equitable authority. These could include orders directing disgorgement of unlawful profits.").

In sum, petitioners err in contending (Pet. 10) that "[t]he precisely-calibrated remedial scheme that Congress put in place * * * does not provide for" disgorgement. Congress repeatedly has made clear that an important and well-established component of that "precisely-calibrated remedial scheme" is the power of the federal courts to require violators like petitioners to surrender their ill-gotten gains. Under these circumstances, it is petitioners' argument that threatens the proper boundaries between the legislative and judicial roles by inviting courts to ignore express congressional affirmation of and reliance on established judicial constructions of Acts of Congress and by lightly presuming a congressional intent to deny courts their inherent and long-recognized authority to order ancillary equitable relief.[11]

2. Petitioners also argue (Pet. 22-25) that, even if the remedy of disgorgement is available, the court of appeals erred in holding that Brennan is jointly and severally liable for the entire disgorgement amount. The court's ruling was correct and rested on the specific facts of this case, making further review unwarranted.

a. Section 20(a) of the Exchange Act, 15 U.S.C. 78t(a), expressly imposes joint and several liability on control persons, and petitioners do not question the court's finding that petitioner Brennan is liable as a

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[11] This Court has already rejected petitioners' additional contention (Pet. 19) that disgorgement is unavailable because the statutory injunctive remedy is forward-looking. See, *e.g.*, *Mills*, 396 U.S. at 386 (finding no merit to contention that equitable remedies under the Exchange Act are limited to prospective relief).

control person. Nor do petitioners contest that joint and several liability attaches in civil actions brought by the Commission. See Exchange Act, § 3(a)(9), 15 U.S.C. 78c(a)(9) (defining the term "person[s]," who can recover joint and several liability under Section 20(a), to include the Commission). Most of petitioners' objections about the supposed unfairness of imposing liability in this case thus simply reflect a disagreement with Congress's decision to impose joint and several liability on control persons. That, however, is an insufficient basis for this Court's review.

b. Petitioners assert (Pet. 23) that the court's imposition of liability on Brennan creates a circuit conflict by allowing disgorgement beyond the profits actually received. Petitioners are mistaken. No court has held that joint and several liability is inappropriate when a defendant has sole and complete operational and financial control over a company and has been found primarily and individually liable for each of the securities violations at issue. In fact, petitioners do not even identify a case that is factually analogous to the present case. There is thus no basis for believing that this case would have been resolved differently in any other circuit.

Petitioners' argument, moreover, is predicated upon an unduly restrictive view of the benefits Brennan received from the fraudulent venture. Although petitioners repeatedly assert (Pet. 3, 24, 25) that Brennan received less than $1 million from his illegal conduct, in fact, as they admit (Pet. 4), he received approximately $14 million in cash compensation from First Jersey during 1982-1985 alone. Pet. App. 130a. Brennan also received many millions more in cash

benefits from First Jersey.[12] Additionally, throughout the time of the fraudulent transactions (and beyond), Brennan's single-handed dominion over First Jersey allowed him to withdraw any amount of money from the firm at any time he desired. *Id.* at 40a.[13] The ready availability of this money meant that Brennan benefitted directly from any increase in the worth of the firm that arose from the wrongful conduct. *Ibid.* Further, the district court chronicled the extensive financial dealings (in the millions of dollars) that benefitted Brennan in the wake of defrauding First Jersey's investors (*id.* at 85a-93a), and concluded that "[n]one of this would in all probability have been achievable by him without the income produced by the illegal markups and what those sums enabled him and First Jersey to further obtain" (*id.* at 101a). Because the financial benefits Brennan received from the wrongdoing were so substantial and enduring, far exceeding what petitioners are willing to acknowledge, the court's order that Brennan be held liable for the entire disgorgement amount was appropriate. See *Blavin*, 760 F.2d at 713 ("Disgorgement orders are not limited to confiscation of trading profits," and may reach other financial benefits received by the wrongdoer.).

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[12] Petitioners ignore the $6.7 million that Brennan withdrew from the firm in 1986-1987 (which brought Brennan's total withdrawals for 1982-1987 to $20,700,694, see Pet. App. 130a); Brennan's receipt of $5 million for his "covenant not to compete" upon the sale of the bulk of First Jersey's retail offices in 1987 (Tr. 5616-5631 (Oct. 12, 1994)); and the millions of dollars that First Jersey paid out after 1987 to Brennan and for Brennan's benefit (Tr. 5431-5434 (Oct. 6, 1994)).

[13] In 1991, First Jersey spent $4.3 million to purchase securities for Brennan. Pet. App. 179a.

c. Petitioners are also incorrect in asserting (Pet. 25-27) that there is a circuit conflict concerning the right to a jury trial or the applicability of a statute of limitations in this case. As an initial matter, petitioners are in no position to raise a claim to a jury trial. The district court ruled that, assuming defendants were entitled to a jury, they had "waived their right" by failing to make a timely demand. C.A. App. 387-388 (noting that five years of pretrial preparation elapsed before petitioners requested a jury).

In any event, petitioners' arguments rest on the erroneous premise that the ordered disgorgement of unlawful profits is a penalty. While petitioners cite numerous cases supporting the unremarkable proposition that penalties are subject to the right to jury trial and applicable statutes of limitation, petitioners identify no case holding that the disgorgement of ill-gotten gains is a penalty, much less that it is a penalty to require one who orchestrated an unlawful scheme to disgorge fraudulently obtained funds over which he had complete control and which directly increased his net worth. See *United States* v. *Ursery*, 116 S. Ct. 2135, 2148-2149 (1996) (forfeiture of the proceeds of illegal activity serves the "nonpunitive goal of ensuring that persons do not profit from their illegal acts"); *SEC* v. *First City Financial Corp.*, 890 F.2d 1215, 1231 (D.C. Cir. 1989) (disgorgement is not penal as long as the amount is causally connected to the wrongdoing).

Petitioners also challenge (Pet. 25) the rate of prejudgment interest awarded. Petitioners' fraud essentially provided them with an unsecured, interest-free loan of the illegal profits they have been ordered to disgorge. The Internal Revenue Service underpayment interest rate, which the court applied, is a

reasonable approximation of the amount defendants would have had to pay for an unsecured loan of the amount obtained through fraud, because the underpayment rate conforms to the prevailing level of interest rates in the economy. See H.R. Rep. No. 426, 99th Cong., 1st Sess. 849 (1985); S. Rep. No. 313, 99th Cong., 2d Sess. 184 (1986).[14]

To be sure, the amount required to be disgorged in this case is large, but the fraud was immense and long lasting, and the unlawful profits large. Far from

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[14] Petitioners are incorrect in asserting that the Commission has acknowledged that "any funds obtained through disgorgement will be paid to the U.S. Treasury and *not* to the victims of the alleged fraud" (Pet. 5, 17). Petitioners' transcript citations do not support their assertion. The Commission's well-established position is that the primary purpose of disgorgement is to deter violations by depriving wrongdoers of their ill-gotten gains, not to compensate victims. See also *Ursery*, 116 S. Ct. at 2148-2149; *Randall* v. *Loftsgaarden*, 478 U.S. 647, 663 (1986) ("[I]t is more appropriate to give the defrauded party the benefit even of windfalls than to let the fraudulent party keep them."); *Jackson* v. *Smith*, 254 U.S. 586, 588-589 (1921) (imposing joint and several liability on a receiver and his associates to account for all profits made by them through self-dealing in assets of a trust estate, even though "the estate may not have been injured" by their misconduct). Once the money is recovered, however, the Commission generally seeks to restore those funds to the victims through a court-approved distribution plan if they received less than full recovery in any private litigation brought on their behalf. Alternatively, the funds are sometimes paid into the Treasury. See generally *SEC* v. *Wang*, 944 F.2d 80, 81-82 (2d Cir. 1991); Paul Gonson & Randall Quinn, *The Disgorgement Dilemma: Who Gets the Money Recovered by the SEC in Insider Trading Cases?*, 35 Fed. B. News & J. 192 (1988). In any event, petitioners' complaint is premature because the district court has not yet approved any plan for distribution of the disgorged funds in this case.

being a ground for extending Brennan special consideration, the enormity of Brennan's wrongdoing and of the financial benefits he reaped from the scheme fully justifies the remedial decree entered.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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